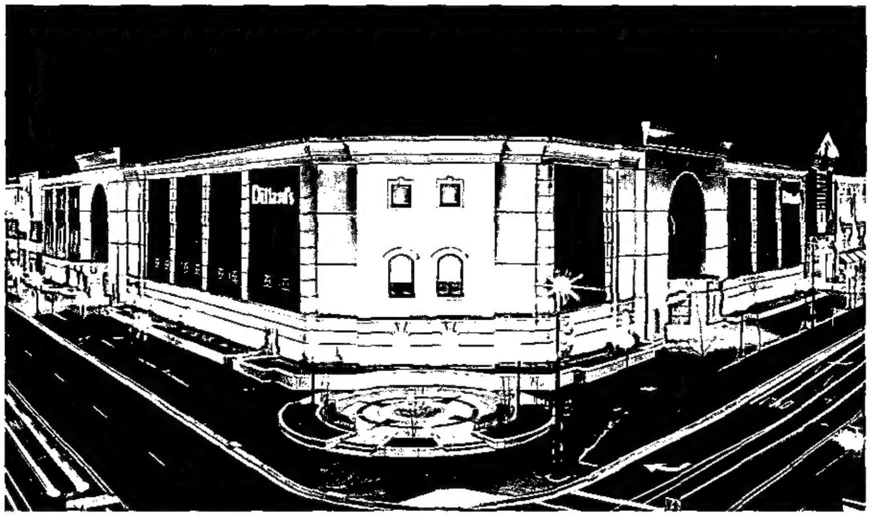
1998 HAS BEEN THE MOST EXCITING AND PIVOTAL YEAR
IN OUR COMPANY'S 60-YEAR HISTORY.

Challenge & Opportunity



DILLARD'S, INC. 1998 ANNUAL REPORT

Dillard's Corporate Profile

Sixty years ago, William Dillard established the first Dillard's store in Nashville, Arkansas. From this humble beginning, the Company has emerged as one of the most successful retail chains in the United States, with annual sales of more than $7.8 billion.

Today, Dillard's, Inc. comprises 328 traditional stores and seven clearance centers in 29 states, offering a distinctive mix of name-brand and private-label merchandise. With everyday value pricing and special emphasis on fashion apparel and home furnishings, Dillard's appeals to a broad range of consumers.

The Company's philosophy continues to embrace an ambitious program of expansion and remodeling, as well as aggressive response to industry trends in merchandising and pricing.

Dillard's Merchandising Philosophy

Dillard's caters to a broad cross-section of the population in our respective markets. Our merchandise emphasis is on branded goods, both in fashion apparel and home furnishings.

By carrying branded merchandise in a range of price levels – moderate and better – we create a fashion image designed to appeal to the maximum number of customers.

Our competitive leadership is based on these:

1. Presenting fashion and trends as they emerge, capitalizing on being the first in our areas to offer such merchandise.
2. Offering a strong basic stock consistently, so that customers can always find their staple fashion and home furnishing needs, and thus think of Dillard's as the place to go for all their families' needs.
3. Keeping stores fully stocked in both fashion and basic merchandise.

Particularly, we strive to have the right goods at the right price, at the right time – without sacrificing any of those concepts for promotional gain. Our merchandise should be recognizable as branded, supplemented with quality goods marketed under the Dillard's label.

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Financial Highlights

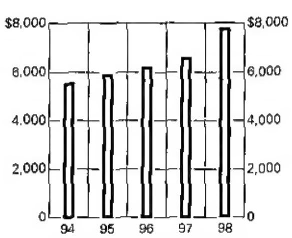
1998 ANNUAL REPORT

IN THE MOST EXCITING AND PIVOTAL YEAR IN DILLARD'S 60-YEAR HISTORY, THE COMPANY ACHIEVED RECORD NET SALES FOR 1998.

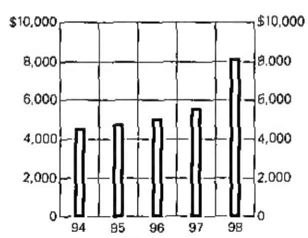
Selected Financial Highlights

(dollars in thousands, except per share amounts)	**1998**	1997	1996	1995	1994
Income Statement Data:					
Net sales	**$7,796,741**	$6,631,752	$6,227,585	$5,918,038	$5,545,803
Net income	**135,259**	258,325	283,621	167,183	251,790
Diluted earnings per common share	**1.26**	2.31	2.09	1.48	2.23
Balance Sheet Data:					
Current assets	**$3,437,711**	$2,998,057	$2,760,636	$2,658,225	$2,524,802
Current liabilities	**1,093,802**	1,098,850	894,746	869,680	758,958
Long-term debt	**3,002,595**	1,365,716	1,173,018	1,157,864	1,178,503
Guaranteed Preferred Beneficial Interests in the Company's Subordinated Debentures	**531,579**	—	—	—	—
Stockholders' equity	**2,841,522**	2,807,938	2,717,178	2,478,327	2,323,567
Operational Data:					
Number of stores	**335**	270	250	238	229
Number of employees	**54,921**	44,616	43,470	40,312	37,832
Gross square footage (in thousands)	**55,000**	43,000	40,000	37,300	35,300

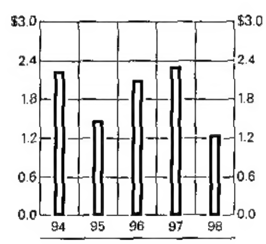
Net Sales
(in millions)



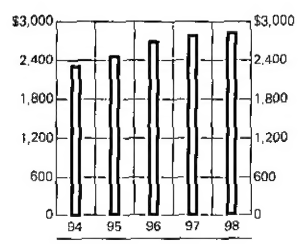
Total Assets
(in millions)



Diluted Earnings per Share
(in dollars)



Stockholders' Equity
(in millions)



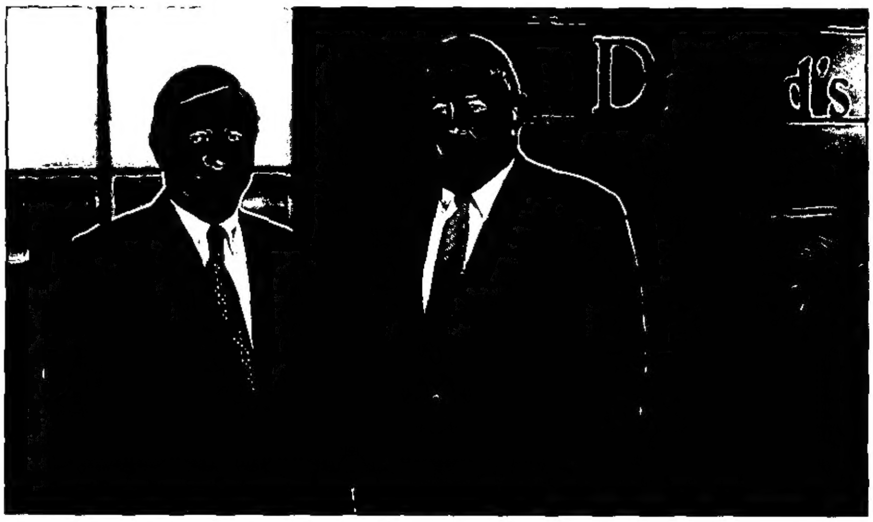
DILLARD'S, INC.

CAPITALIZING ON CONTINUING INDUSTRY CONSOLIDATION, DILLARD'S AGGRESSIVELY MET THE CHALLENGE TO REMAIN COMPETITIVE.

Dear Shareholder,

1998 has been the most exciting and pivotal year in Dillard's 60-year history. We had clearly reached a strategic turning point in our ongoing development as a major player in the retail industry, and the continuing consolidation in the broadline retail sector presented us with both challenge and opportunity. The challenge: remaining competitive in an environment where size matters and relationships with valued vendors increasingly affect relationships with valued customers. The opportunity: seeking out ways to capitalize on this industry consolidation, utilizing both our financial strength and experience in acquiring and integrating stores into our network.

In the spring of 1998, the opportunity to purchase Mercantile Stores Company, Inc. arose — and we were ready. Based in Fairfield, Ohio, Mercantile operated 106 department stores and 16 home fashion stores spanning 17 states. We had admired this operation for many years, both as respected retail managers and formidable competitors. On May 18, 1998, we announced a tender offer of $80 per share for the outstanding shares of Mercantile Stores Company, Inc., and completed the acquisition three months later on August 13, 1998. We remain confident that this was by far the best thing we could do for our shareholders, our Company and our associates. The time was right. The opportunity was right. And all financial and operational aspects of such an undertaking were measured and carefully considered. The answer was clear: this was right for the future of Dillard's.



Alex Dillard
President

William Dillard, II
Chief Executive Officer

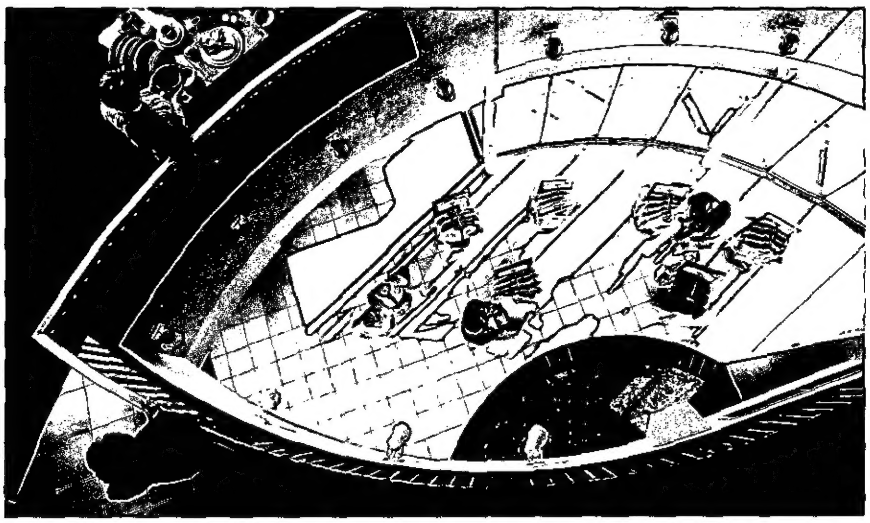
CONSIDERED THE JEWEL OF POTENTIAL ACQUISITIONS, MERCANTILE MAINTAINED THE NUMBER-ONE POSITION IN 70 PERCENT OF ITS MARKETS.

The Time Was Right

The timing of the Mercantile opportunity could not have been better. By the spring of 1998, we had purchased $275 million of the $300 million authorized under our Share Repurchase Plan which was approved by the Board of Directors in February 1997. Our Company was financially strong with favorable cash flow and a low debt-to-equity position. We had reached a crossroads on further driving shareholder value when the Mercantile opportunity enabled us to capitalize on our strengths and maximize our Company's potential.

The Opportunity Was Right

The location of the Mercantile stores offered a great fit for integration into our existing network. Operating in both urban and less-urban areas as we do, they had maintained the number-one position in over 70 percent of their markets. Some experts had dubbed Mercantile "the jewel" of potential acquisitions in our industry — and we strongly shared that belief. The locations gave us opportunities to enter several new markets and to expand our presence in existing markets. We added our 29th state with three new locations in Montana, and greatly increased our presence in Alabama, Florida and Ohio, among other states. In addition, we strengthened our position in attractive markets such as Denver, Colorado, and Nashville, Tennessee.



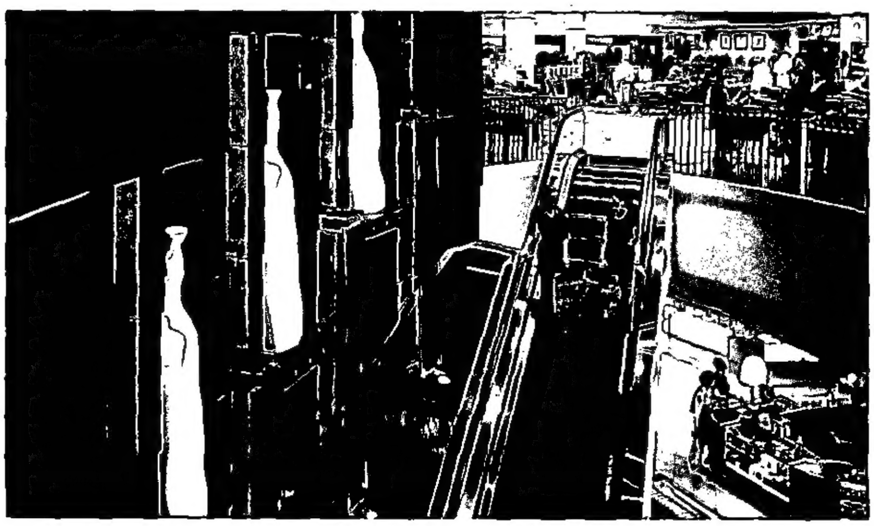
The former Southglenn Mall Mercantile store in the Denver suburb of Littleton, Colorado, combines open inviting expanses with dramatic architectural detailing.

THE ADDITION OF MERCANTILE ENABLES DILLARD'S TO ENTER NEW MARKETS AND EXPAND ITS PRESENCE IN EXISTING MARKETS.

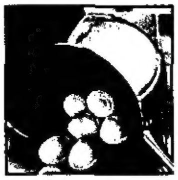
Financial and Operational Considerations

As broadline retail consolidation continues, the need for critical mass becomes more apparent to us. At year-end 1997, we operated 270 stores across 27 states with 43.3 million square feet of selling space. Despite this accomplishment, we recognized the need to place ourselves in the top tier of our industry. The acquisition of Mercantile is just what we needed to achieve that objective. Dillard's now ranks among the top three fashion apparel retailers in the country, boasting 328 traditional stores spanning 29 states and offering 55 million square feet of space, an increase of 27 percent. Operating behind the largest nameplate in the fashion apparel industry, we are now firmly in the top tier and are firmly committed to continued progress.

The locations of the former Mercantile stores, as mentioned above, were remarkably attractive considering the regions in which we operated and the markets in which we desired to operate. As expected with an acquisition of this size, some stores did not fit within our strategy, mainly because of overlap with existing Dillard's locations. Rather than a liability, we saw this as an opportunity. We were well aware of the value of these locations, as were other retailers. In two agreements, we sold 26 locations and realized proceeds of approximately $1 billion, in line with our best expectations. In another transaction, we swapped seven former Mercantile locations for nine new locations, including eight sites in Virginia, a region of exciting potential for us going forward.



Bold and beautiful styling accents the interior of the former Mercantile store in Littleton, Colorado.



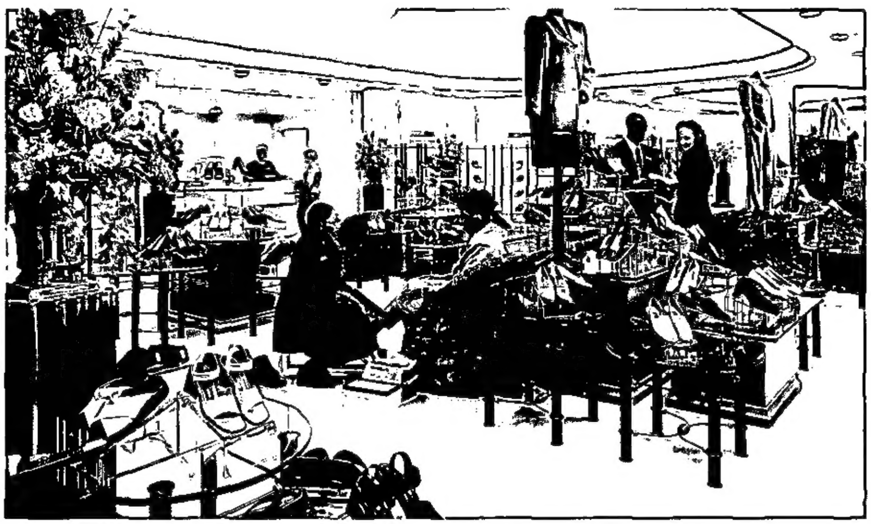
WITH 328 TRADITIONAL STORES IN 29 STATES, DILLARD'S NOW RANKS AMONG THE TOP THREE FASHION APPAREL RETAILERS IN THE COUNTRY.

Among the greatest financial benefits of the Mercantile opportunity is one of the least measurable at this point – enhanced buying power. We never underestimate the effect of valued vendor relationships on our business and strive to develop and nurture these associations. Just as we expect excellence from our vendors, they expect excellence from us in return. Quite simply, we now have more to offer our vendors – namely, our greatly expanded buying needs, additional square footage in which to promote their merchandise, more associates to learn and market their products, and increased advertising opportunities. Likewise, we now have more to offer our customers – more of the merchandise they desire, delivered at exceptional value.

In combining the two companies, we have recognized a tremendous opportunity for cost savings. By quickly eliminating duplicate operations corporate-wide – from merchandising and distribution to corporate overhead functions – we have put into place a solid platform from which to capitalize on these synergies. We have been excited about this aspect of the acquisition from the beginning, and we continue to view these cost-savings opportunities as extremely compelling.

Integration

The integration of the former Mercantile stores continues. We are quite pleased with the effort to date, and to a large degree, the most challenging portion is behind us. We assumed operation of the new stores on August 13, 1998, and just over a week later, merged all ongoing



The women's shoe department of the new MacArthur Center Dillard's store offers a spacious and inviting display of merchandise.

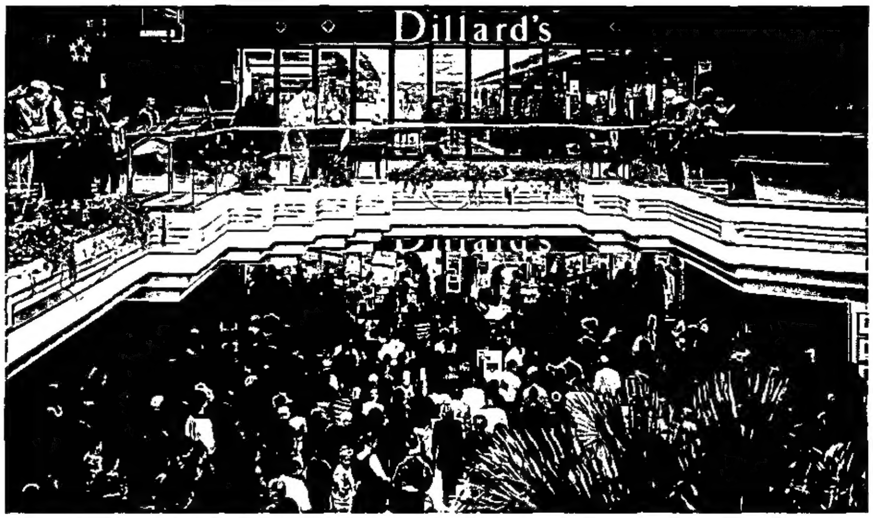
DILLARD'S, INC.

DILLARD'S NOW HAS MORE TO OFFER ITS CUSTOMERS – MORE OF THE MERCHANDISE THEY DESIRE, DELIVERED AT EXCEPTIONAL VALUE.

data processing systems of the new stores with our existing network. As a result of many long weeks of preparation, this conversion proceeded smoothly and is among the many well-planned and well-executed areas of transition.

However, as might be expected in an undertaking of this magnitude, there were some surprises in spite of our best efforts to prevent them – some pleasant and some unpleasant. Our most unpleasant surprise occurred in the area of merchandise distribution. As the Mercantile-ordered merchandise was received, we learned that the receiving system conversion was not adequate. This disruption delayed a substantial amount of fall merchandise from reaching our stores in time for maximum initial sell-though, affecting our core Dillard's locations as well as the newly acquired stores. We reacted to this problem quickly and decisively, and by mid-December our distribution process was largely back on track.

On a more pleasant note, we were extremely pleased with the speed at which the overlapping stores were sold to other retailers. These transactions were negotiated much more quickly than we had originally planned, allowing us to focus on integrating the retained stores even sooner and more effectively. The proceeds we realized from these store sales were in line with our best expectations and enabled us to pay down a significant portion of the debt incurred to finance the acquisition. Additionally, the cost of funds associated with this debt met our best expectations as well.



The March 1999 grand opening of the newly constructed Dillard's store in the Norfolk, Virginia, MacArthur Center attracted an estimated 40,000 eager shoppers.

IN COMBINING THE TWO COMPANIES, DILLARD'S HAS A TREMENDOUS OPPORTUNITY TO CAPITALIZE ON THEIR SYNERGIES AND STRENGTHS.

Learning From Mercantile

We are convinced the former Mercantile operation did many things right. After an open-minded look at Mercantile and an inward look at ourselves, we have adopted many of Mercantile's best practices. One area we admired greatly about them was their success in credit services. Under visionary leadership, they had developed a top-notch credit operation, offering customers a wide array of services from the basic credit card to VIP programs to gift cards. We have retained the leadership talent of this operation and have empowered them to work with our existing credit professionals to develop these programs for all Dillard's customers. In November 1998, we replaced our gift certificate system with the first Dillard's gift card, bringing our customers a much more flexible gift-giving alternative. Other efforts to enhance our credit marketing operation are well underway, and we remain excited about the opportunities there for our customers and for our Company.

We believe our increasingly busy core customer values a little special attention and pampering. Many of the Mercantile stores had achieved tremendous success in meeting this need by offering day spa and hair and nail salon services under one roof. We see the opportunity to develop this further as a highly profitable business, complementing our continuing emphasis on fashion apparel. We have retained the former Mercantile leadership of this area, as well, and

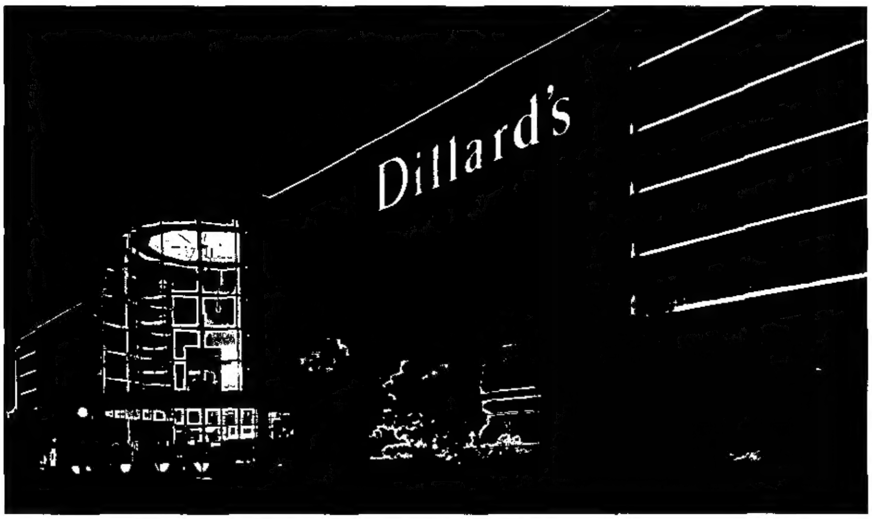
The day spa and hair and nail salon at the new Norfolk, Virginia, store offers special attention and pampering for Dillard's increasingly busy core customer.

DILLARD'S IS QUICKLY ADOPTING MANY OF MERCANTILE'S BEST PRACTICES – FROM CREDIT SERVICES TO BIG AND TALL MENSWEAR.

have charged them to develop this approach further for our Dillard's customers. In fact, our newly constructed Dillard's store in Norfolk, Virginia, which opened in March, offers a wide range of day spa and hair and nail services in a new 2,500-square-foot facility. We are committed to the development of this business and are looking forward to much success in this area.

For many years, the big and tall business of Mercantile has served the special size needs of larger male shoppers. We view this well-executed merchandising area with a continually profitable return as an exciting opportunity for the ongoing combined business. Currently, we are planning to roll the big and tall business into our existing Dillard's stores, as well as maintain the position in the former Mercantile stores. By mid-fall 1999, we hope to offer big and tall in all areas of the men's store in approximately 200 locations, and ultimately to offer these special sizes in the large majority of our stores.

While the Mercantile acquisition and integration were underway in 1998, we successfully opened eight new stores in strategic markets and remodeled several of our most promising locations. The opening of our Boise Towne Square store in Boise, Idaho, gave us a foothold in a new state, and we look forward to serving our new Idaho customers.



Dillard's presence in the attractive Denver market is being strengthened by former Mercantile stores including the Southglenn Mall store in Littleton, Colorado.

DILLARD'S IS DEVELOPING THE DAY SPA BUSINESS AS A HIGHLY PROFITABLE COMPLEMENT TO ITS EMPHASIS ON FASHION APPAREL.

Our Ongoing Focus

As we go forward, our focus will remain on the continued and successful integration of our newly acquired stores. Indeed, many of them now reflect the inventory selection and approach to merchandising our customers have come to expect of us. We anticipate full integration in all units by the fall of the current year.

We appreciate and applaud the long hours and hard work our associates have invested in the Mercantile acquisition. The teamwork displayed company-wide has been remarkable. We welcome our new associates from the former Mercantile operation to our Company and look forward to many years of mutually profitable partnership.

Although we are now a much larger and more complex company, our purpose remains as simple as it was 60 years ago – superior service and exceptional value for our customers. In closing, we want to reiterate our continuing belief that the Mercantile acquisition and the steps we took to grow Dillard's in 1998 were by far the best thing we could do for our shareholders, our associates and our Company. We remain excited about the future of Dillard's.

William Dillard II

William Dillard, II
Chief Executive Officer

Alex Dillard

Alex Dillard
President

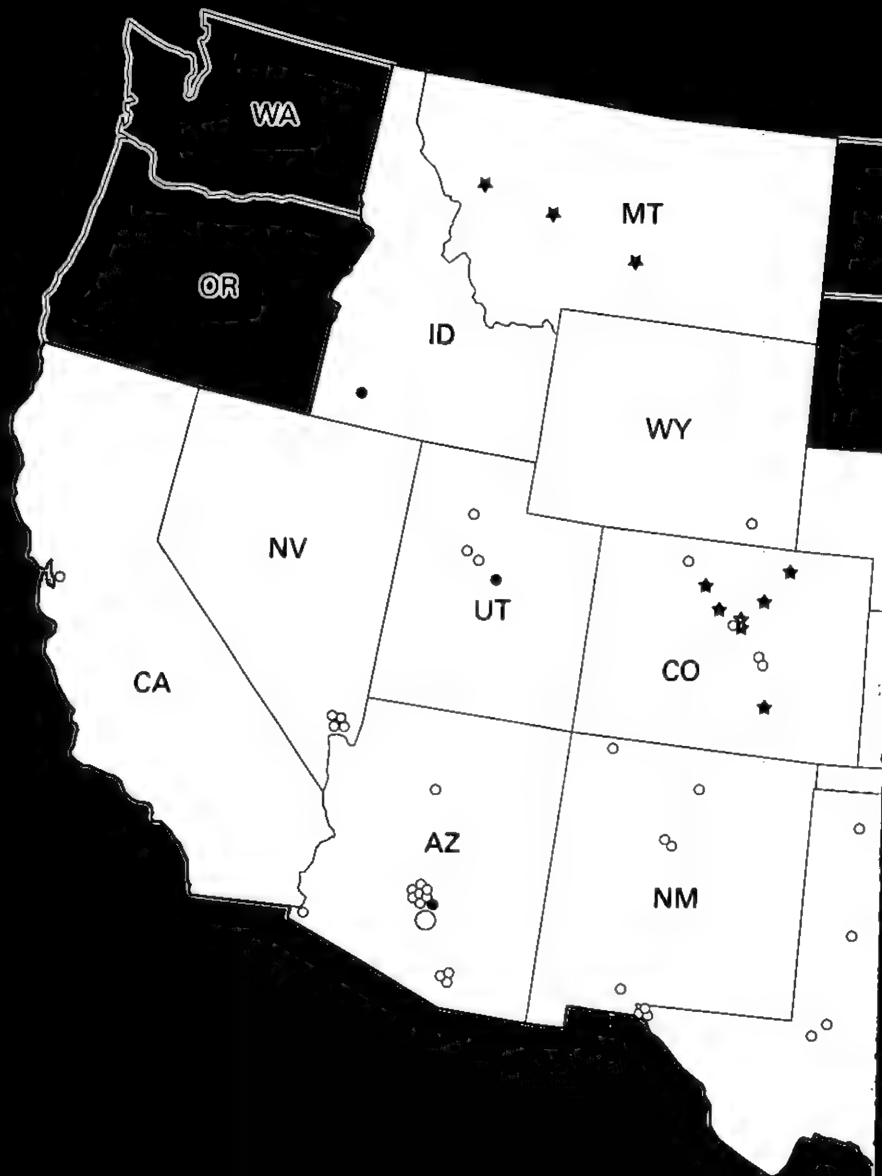
DILLARD'S, INC.

MONTANA WAS ADDED AS OUR 29TH STATE WITH THREE NEW LOCATIONS IN THE CITIES OF MISSOULA, HELENA AND BILLINGS.

In Ohio, we acquired 11 new locations. This is an increase of 2,000,000 square feet.

In Kentucky, we acquired seven new locations. This is an increase of 1,800,000 square feet.

In Alabama, we acquired 11 new locations to add to our existing location. This is an increase of 1,700,000 square feet.



1998 ANNUAL REPORT

WE SWAPPED SEVEN FORMER MERCANTILE LOCATIONS FOR NINE NEW LOCATIONS, EIGHT OF WHICH WERE IN VIRGINIA, A REGION OF EXCITING POTENTIAL FOR US GOING FORWARD.

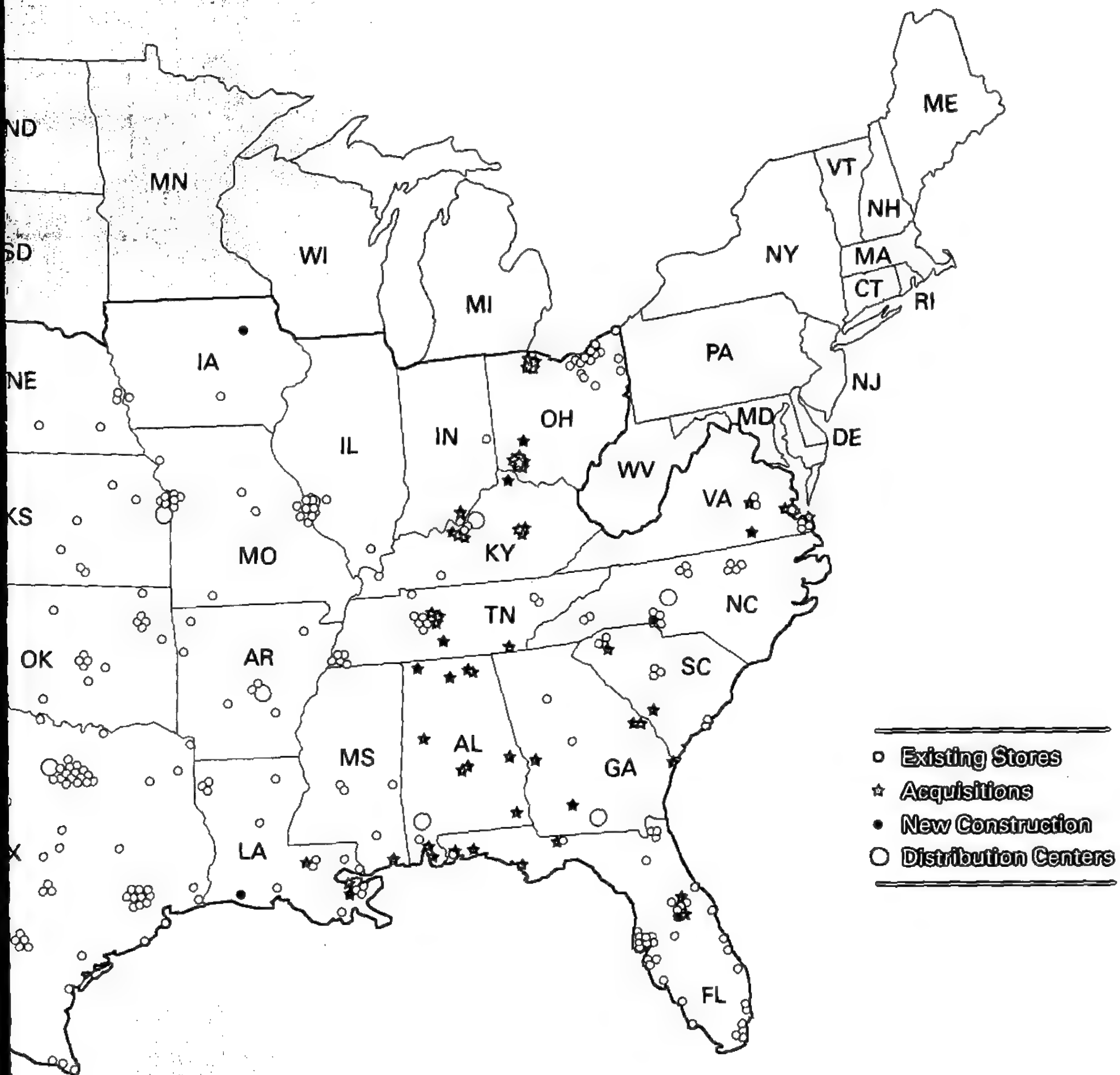
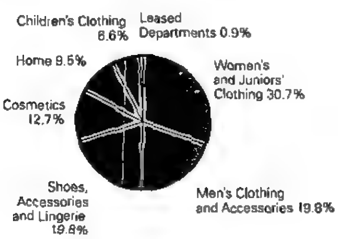


TABLE OF SELECTED FINANCIAL DATA

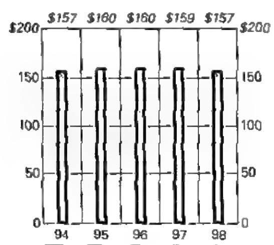
(in thousands, except share and per share amounts)	1998	1997	1996
Net sales	**$ 7,796,741**	$ 6,631,752	$ 6,227,585
Percent increase	**18%**	6%	5%
Cost of sales	**5,218,095**	4,393,291	4,124,765
Percent of sales	**66.90%**	66.20%	66.20%
Interest and debt expense	**196,680**	129,237	120,599
Income before taxes	**219,084**	410,035	378,761
Income taxes	**83,825**	151,710	140,140
Net income	**135,259**	258,325	238,621
Per Common Share			
Diluted earnings per share	**1.26**	2.31	2.09
Dividends	**0.16**	0.16	0.14
Book value	**26.57**	25.70	23.91
Average number of shares outstanding	**107,636,260**	111,993,814	113,988,633
Accounts receivable	**1,230,059**	1,186,491	1,154,673
Merchandise inventories	**2,157,010**	1,784,765	1,556,958
Property and equipment	**3,684,629**	2,501,492	2,191,933
Total assets	**8,177,559**	5,591,847	5,059,726
Long-term debt	**3,002,595**	1,365,716	1,173,018
Capitalized lease obligations	**27,000**	12,205	13,690
Deferred income taxes – total	**700,727**	314,971	261,094
Guaranteed Preferred Beneficial Interests in the Company's Subordinated Debentures	**531,579**	—	—
Stockholders' equity	**2,841,522**	2,807,938	2,717,178
Number of employees – average	**54,921**	44,616	43,470
Gross square footage (in thousands)	**55,000**	43,300	40,000
Number of Stores			
Opened	**5**	12	15
Acquired	**65**	11	0
Closed	**5**	3	3
Total – end of year	**335**	270	250

* 53 Weeks

Sales by Merchandise Category
(percentage of total sales)



Sales per Average Square Foot
(in thousands)



Long-term Debt to Capitalization
(percentage)

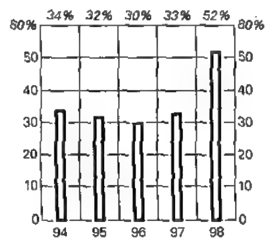
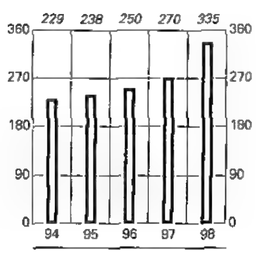


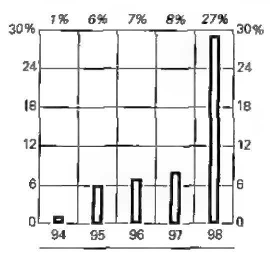
TABLE OF SELECTED FINANCIAL DATA

1995*	1994	1993	1992	1991	1990	1989*
$ 5,918,038	$ 5,545,803	$ 5,130,648	$ 4,713,987	$ 4,036,392	$ 3,605,518	$ 3,049,062
7%	8%	9%	17%	12%	18%	19%
3,893,786	3,614,628	3,306,757	3,043,348	2,565,904	2,287,891	1,926,971
65.80%	65.20%	64.40%	64.50%	63.60%	63.50%	63.20%
120,054	124,282	130,915	121,940	109,386	97,032	91,836
269,653	406,110	399,534	375,330	322,157	280,778	227,892
102,470	154,320	158,400	138,900	116,000	98,000	79,800
167,183	251,790	241,134	236,430	206,157	182,778	148,092
1.48	2.23	2.14	2.11	1.84	1.67	1.45
0.12	0.10	0.08	0.08	0.07	0.07	0.06
21.91	20.55	18.42	16.28	14.19	12.31	10.23
113,143,842	113,013,998	112,808,262	112,292,575	111,832,758	109,351,914	101,890,272
1,123,103	1,117,411	1,111,744	1,106,710	1,004,496	932,544	759,803
1,486,045	1,362,756	1,299,944	1,178,562	1,052,683	889,333	716,054
2,035,538	1,984,145	1,921,470	1,688,682	1,338,434	1,088,753	921,820
4,778,535	4,577,757	4,430,274	4,107,114	3,498,506	3,007,979	2,496,277
1,157,864	1,178,503	1,238,293	1,381,676	1,008,967	839,490	739,597
20,161	22,279	31,621	32,381	29,489	31,284	32,900
248,469	302,801	284,981	178,311	143,463	115,854	108,426
—	—	—	—	—	—	—
2,478,327	2,323,567	2,081,647	1,832,018	1,583,475	1,364,885	1,094,721
40,312	37,832	35,536	33,883	32,132	31,786	26,304
37,300	35,300	34,900	33,200	29,100	26,600	23,500
9	7	10	11	10	4	3
0	0	0	12	7	23	19
0	5	1	3	5	3	6
238	229	227	218	198	186	162

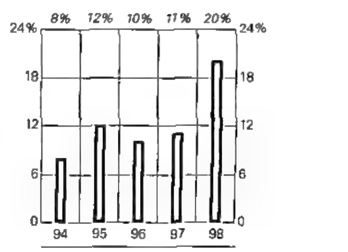
Total Number of Stores



Growth in All Store Square Footage (annual percentage increase)



Growth in Owned Store Square Footage (annual percentage increase)



MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Dillard's, Inc. and Subsidiaries

Acquisition

During fiscal 1998, the Company completed its acquisition (the "Acquisition") of Mercantile Stores Company, Inc. ("Mercantile") for approximately $3 billion in cash. Mercantile was a conventional department store retailer engaged in the general merchandising business, operating 106 department and home fashion stores under 13 different names in a total of 17 states.

The Acquisition was accounted for under the purchase method and, accordingly, the results of operations have been included in the Company's results of operations since August 13, 1998, and the purchase price has been allocated to Mercantile's assets and liabilities based on their estimated fair values as of that date. The excess of cost over net assets acquired is approximately $666 million.

In connection with the Acquisition, the Company entered into two separate agreements whereby the Company sold in the aggregate 26 of the acquired stores to Proffitt's, Inc. and The May Department Stores Company. In addition, the Company entered into an agreement with Belk, Inc. to exchange seven of the acquired stores for nine Belk, Inc. stores. The results of operations of the sold or exchanged stores are included in the accompanying statements of operations from the date of acquisition to the date of sale or exchange.

Sales

The sales increases were 18%, 6% and 7% for 1998, 1997 and 1996, respectively. The sales increase for 1998 is primarily attributable to the Acquisition. The comparable store sales increase was 1% for 1998 and 2% for 1997 and 1996, respectively. Comparable store sales include sales for those stores which were in operation for a full period in both the current month and the corresponding month for the prior year.

Management believes that the majority of the increase in sales in comparable stores was attributable to an increase in the volume of goods sold rather than an increase in the price of goods.

The sales mix for the past three years by category as a percent of total sales has been:

	1998	1997	1996
Cosmetics	**12.7%**	12.7%	12.9%
Women's and Juniors' Clothing	**30.7**	30.6	29.9
Children's Clothing	**6.6**	6.4	6.5
Men's Clothing and Accessories	**19.8**	19.5	19.5
Shoes, Accessories and Lingerie	**19.8**	20.2	19.9
Home	**9.5**	10.2	10.8
Leased Departments	**.9**	.4	.5
Total	**100.0%**	100.0%	100.0%

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Dillard's, Inc. and Subsidiaries

Cost of Sales

Cost of sales as a percentage of sales was 66.9%, 66.2% and 66.2% for 1998, 1997 and 1996, respectively. Cost of sales for fiscal 1998 includes a charge of $39 million for inventory valuation adjustments resulting from the alignment of Mercantile inventories to reflect the Company's merchandising and pricing philosophy. Additionally, during the fourth quarter of 1998, the Company experienced significant merchandise processing and distribution delays due to systems integration problems during consolidation of the Dillard and Mercantile distribution systems. The delays resulted in later than planned store receipts and subsequent higher levels of markdowns in the post-holiday selling season.

Expenses

Expenses as a percentage of sales for the past three years were as follows:

	1998	1997	1996
Advertising, selling, administrative and general expenses	**26.6%**	24.6%	24.7%
Depreciation and amortization	**3.1**	3.0	3.1
Rentals	**.9**	.8	.9
Interest and debt expense	**2.5**	2.0	2.0

Included in advertising, selling, administrative and general expenses ("SG&A") for fiscal 1998 were certain business integration and consolidation expenses ("BICE") associated with the integration of Mercantile into the Company. BICE included $43 million of severance costs, $26 million of lease rejection costs for facilities closed subsequent to the Acquisition and $22 million of costs associated with operating Mercantile central office functions for a transitional period. Excluding such charges, SG&A expenses as a percentage of net sales were 25.4% for fiscal 1998. The Company is continuing the process of consolidating various administrative support functions such as marketing, buying, advertising, accounting and management information systems, as well as aligning store operating and distribution methodologies. The Company estimates that SG&A expenses for fiscal 1998 included additional payroll and other systems integration expenses of approximately $30 million primarily relating to transitional distribution cost incurred to process Mercantile-ordered merchandise in Dillard's receiving systems. The Company has taken steps to reduce payroll and other overhead expenses, and expects to achieve cost reductions as a result of a more efficient overhead expense structure and to increase purchasing power derived from the combination of the two companies. SG&A expenses decreased as a percentage of sales during fiscal 1997 primarily due to a reduction in bad debt expense, offset by an increase in payroll expense. Payroll expense in the selling area increased as a percentage of sales in fiscal 1997 as the Company sought to invest more in its sales force. Depreciation and amortization increased slightly as a percentage of sales during 1998. This increase is primarily due to the amortization of goodwill related to the Acquisition. Rentals increased slightly as a percentage of sales during fiscal 1998 reflecting the relatively higher percentage of leased property of Mercantile. A higher level of borrowing due to the Acquisition caused the increase in interest and debt expense as a percentage of net sales for fiscal 1998.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Dillard's, Inc. and Subsidiaries

Liquidity and Capital Resources

Net cash flows from operations were $643 million for 1998. In addition to cash flows from operations, the Company borrowed $1,650 million by issuing unsecured notes in underwritten public offerings and borrowed $200 million by issuing Capital Securities in an underwritten public offering. A subsidiary of the Company issued $332 million in preferred stock during the year. These borrowings were used primarily to fund the Acquisition.

Capital expenditures were $248 million for 1998. During 1998, the Company constructed seven new stores (two of which were replacement stores) and expanded and remodeled four stores. During 1998, the Company repaid $134 million of its long-term debt and capitalized lease obligations and repaid $419 million in commercial paper.

In February 1997, the Company announced that the Board of Directors had authorized the implementation of a Class A common share repurchase program of up to $300 million. As of January 30, 1999, the Company has purchased 8,059,700 shares of Class A Common Stock at a cost of $275 million.

During 1998, the Company's merchandise inventories increased by $372 million, primarily due to the Acquisition and the store expansions discussed above. On a comparable store basis, the merchandise inventories were flat. During 1998, the Company transferred all of its credit card receivables to a trust in exchange for a certificate representing an undivided interest in the trust. The Company then sold a certificate with a market value of $300 million to a third party.

For 1999, the Company plans to construct eight stores (two of which will be replacement stores) and expand two stores. Capital expenditures are projected to be approximately $200 million for 1999. Maturities of the Company's long-term debt over the next five years are $164 million, $108 million, $209 million, $110 million and $160 million, respectively.

The Company and its wholly-owned finance subsidiary, Dillard Investment Company, have a revolving line of credit in the amount of $750 million. The revolving line of credit requires that consolidated stockholders' equity be maintained at $1 billion or more. No funds were borrowed under the revolving line of credit during fiscal 1998. At the end of 1998, the Company had an outstanding shelf registration for securities in the amount of $750 million.

The Company expects to finance its capital expenditures and its working capital requirements including required debt repayments from cash flows generated from operations and by issuing new debt.

Quantitative and Qualitative Disclosures About Market Risk

The table below provides information about the Company's obligations that are sensitive to changes in interest rates. The table presents maturities of the Company's long-term debt and Guaranteed Beneficial Interests in the Company's Subordinated Debentures along with the related weighted average interest rates by expected maturity dates.

	Expected Maturity Date (fiscal year)							
(dollar amounts in thousands)	**1998**	1999	2000	2001	2002	Thereafter	Total	Fair Value
Long-term debt	**$164,289**	$108,012	$208,985	$109,913	$160,407	$2,415,278	$3,166,884	$3,321,827
Average interest rate	**7.3%**	9.3%	6.9%	7.5%	6.4%	7.1%	7.1%	
Guaranteed Beneficial Interests in the Company's Subordinated Debentures	**$ —**	$ —	$ —	$ —	$ —	$ 531,579	$ 531,579	$ 532,059
Average interest rate	**—%**	—%	—%	—%	—%	6.9%	6.9%	

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Dillard's, Inc. and Subsidiaries

Year 2000 Readiness Statement

The Company is actively addressing the issues related to the date change in year 2000. This is necessary because many computer systems were written using only two digits to contain the year in date fields. On January 1, 2000, many of these programs will fail to perform date calculations correctly and produce erroneous results. This could temporarily prevent the Company from processing business transactions. The Company began efforts as early as 1996 to address this issue.

Currently, all computer systems including both IT and non-IT systems have been assessed and work is well underway to remediate the systems that are not year 2000 compliant. The non-IT systems are primarily systems with embedded processors such as telephone and security systems. The non-IT systems have substantially been remediated. Approximately 80% of the IT systems have been remediated or were originally developed as year 2000 compliant. The remediation of the remaining IT systems is expected to be complete no later than the second quarter of 1999 with the exception of two systems. These two systems are expected to be complete by the end of August. The Company has obtained letters of certification from its mission-critical computer systems and software vendors.

The external cost (payments to equipment and service vendors) of remediating non-compliant systems incurred thus far is approximately $1.2 million. The Company believes the external cost to remediate all systems will not exceed $2.5 million in total. Additionally, the Company has incurred and will continue to incur internal costs in its remediation process. These internal costs relate principally to the payroll costs of the information systems group and other costs related to the normal operation of the Company's data centers. The Company does not track these costs separately. All costs associated with year 2000 issues will be funded from the Company's existing sources of liquidity.

There are significant risks associated with the year 2000 issues. Many of these risks such as those associated with electrical power and/or telecommunications are outside the reasonable control of the Company. Also, the failure of a significant number of the Company's business partners could have a material impact on the Company's operations. These risks are largely outside the control of the Company. Although the Company believes its remediation and contingency planning efforts adequately identify and address the year 2000 issues that are within the Company's reasonable control, there can be no assurance that the Company's efforts will be fully effective. Due to these significant risks the Company's management is monitoring these efforts very closely. The Audit Committee of the Board of Directors is periodically updated concerning the status of the year 2000 efforts.

Business resumption contingency plans have been completed for the mission-critical systems. These plans address how the Company will continue to do business until the mission-critical system that failed has been remediated. These plans will be periodically reviewed to determine if changing business conditions necessitate a change in the contingency plan.

Forward-Looking Information

The Company cautions that any forward-looking statements (as such term is defined in the Private Securities Litigation Reform Act of 1995) contained in this report, the Company's annual report on Form 10-K or made by management of the Company, involve risks and uncertainties and are subject to change based on various important factors. The following factors, among others, could affect the Company's financial performance and could cause actual results for 1999 and beyond to differ materially from those expressed or implied in any such forward-looking statements: economic and weather conditions in the regions in which the Company's stores are located and their effect on the buying patterns of the Company's customers, changes in consumer spending patterns and debt levels, trends in personal bankruptcies and the impact of competitive market factors.

INDEPENDENT AUDITORS' REPORT

To the Stockholders and Board of Directors of
Dillard's, Inc.
Little Rock, Arkansas

We have audited the accompanying consolidated balance sheets of Dillard's, Inc. and subsidiaries as of January 30, 1999 and January 31, 1998, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended January 30, 1999. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Dillard's, Inc. and subsidiaries as of January 30, 1999 and January 31, 1998, and the results of their operations and their cash flows for each of the three years in the period ended January 30, 1999 in conformity with generally accepted accounting principles.

Deloitte & Touche LLP

New York, New York
March 15, 1999

CONSOLIDATED BALANCE SHEETS

Amounts in Thousands, Except Share Data

Assets	January 30, 1999	January 31, 1998
Current Assets:		
Cash and cash equivalents	$ 72,401	$ 41,833
Accounts receivable (net of allowance for doubtful accounts of $37,487 and $27,809)	1,192,572	1,158,682
Merchandise inventories	2,157,010	1,784,765
Other current assets	15,728	12,777
Total current assets	3,437,711	2,998,057
Property and Equipment:		
Land and land improvements	126,047	36,045
Buildings and leasehold improvements	2,567,943	1,799,072
Furniture, fixtures and equipment	2,624,799	2,125,688
Buildings under construction	38,965	37,691
Buildings under capital leases	50,123	25,148
Less accumulated depreciation and amortization	(1,723,248)	(1,522,152)
	3,684,629	2,501,492
Goodwill (net of accumulated amortization of $7,475)	659,262	—
Other Assets	395,957	92,298
Total Assets	$ 8,177,559	$ 5,591,847

Liabilities and Stockholders' Equity	January 30, 1999	January 31, 1998
Current Liabilities:		
Trade accounts payable and accrued expenses	$ 921,187	$ 530,034
Commercial paper	—	419,136
Current portion of long-term debt	164,289	107,268
Current portion of capital lease obligations	2,396	1,651
Federal and state income taxes	5,930	40,761
Total current liabilities	1,093,802	1,098,850
Long-term Debt	3,002,595	1,365,716
Capital Lease Obligations	27,000	12,205
Deferred Income Taxes	681,061	307,138
Operating Leases and Commitments		
Guaranteed Preferred Beneficial Interests in the Company's Subordinated Debentures	531,579	—
Stockholders' Equity:		
Preferred stock — 4,400 shares issued and outstanding	440	440
Common stock, Class A — 110,966,419 and 110,251,634 shares issued; 102,906,719 and 105,207,134 shares outstanding	1,110	1,103
Common stock, Class B (convertible) — 4,016,929 shares issued and outstanding	40	40
Additional paid-in capital	682,313	657,137
Retained earnings	2,432,793	2,314,709
Less treasury stock, at cost, Class A — 8,059,700 and 5,044,500 shares	(275,174)	(165,491)
Total stockholders' equity	2,841,522	2,807,938
Total Liabilities and Stockholders' Equity	$ 8,177,559	$ 5,591,847

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME

Amounts in Thousands, Except Per Share Data

	Year Ended		
	January 30, 1999	January 31, 1998	February 1, 1997
Net Sales	**$7,796,741**	$6,631,752	$6,227,585
Service Charges, Interest and Other Income	**214,983**	185,157	184,475
	8,011,724	6,816,909	6,412,060
Costs and Expenses:			
Cost of sales	**5,218,095**	4,393,291	4,124,765
Advertising, selling, administrative and general expenses	**2,070,212**	1,629,721	1,538,450
Depreciation and amortization	**239,671**	199,939	193,719
Rentals	**67,982**	54,686	55,766
Interest and debt expense	**196,680**	129,237	120,599
Total costs and expenses	**7,792,640**	6,406,874	6,033,299
Income Before Income Taxes	**219,084**	410,035	378,761
Income Taxes	**83,825**	151,710	140,140
Net Income	**$ 135,259**	$ 258,325	$ 238,621
Basic Earnings Per Common Share	**$ 1.26**	$ 2.32	$ 2.10
Diluted Earnings Per Common Share	**$ 1.26**	$ 2.31	$ 2.09

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

Amounts in Thousands, Except Share and Per Share Data

	Preferred Stock	Common Stock Class A	Common Stock Class B	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Total
Balance, February 3, 1996	$ 440	$1,091	$ 40	$ 625,249	$ 1,851,507	$ —	$ 2,478,327
Issuance of 523,805 shares under stock option, employee savings and stock bonus plans	—	5	–	16,139	—	—	16,144
Net income	—	—	—	—	238,621	—	238,621
Cash dividends declared:							
Preferred stock, $5 per share	—	—	—	—	(22)	—	(22)
Common stock, $.14 per share	—	—	—	—	(15,892)	—	(15,892)
Balance, February 1, 1997	$ 440	$1,096	$ 40	$ 641,388	$ 2,074,214	$ —	$ 2,717,178
Issuance of 657,138 shares under stock option, employee savings and stock bonus plans	—	7	—	15,749	—	—	15,756
Purchase of treasury stock						(165,491)	(165,491)
Net income	—	—	—	—	258,325	—	258,325
Cash dividends declared:							
Preferred stock, $5 per share	—	—	—	—	(22)	—	(22)
Common stock, $.16 per share	—	—	—	—	(17,808)	—	(17,808)
Balance, January 31, 1998	$ 440	$ 1,103	$ 40	$ 657,137	$ 2,314,709	$ (165,491)	$ 2,807,938
Issuance of 714,785 shares under stock option, employee savings and stock bonus plans	—	**7**	—	**25,176**	—	—	**25,183**
Purchase of treasury stock						**(109,683)**	**(109,683)**
Net income	—	—	—	—	**135,259**	—	**135,259**
Cash dividends declared:							
Preferred stock, $5 per share	—	—	—	—	**(22)**	—	**(22)**
Common stock, $.16 per share	—	—	—	—	**(17,153)**	—	**(17,153)**
Balance, January 30, 1999	**$ 440**	**$ 1,110**	**$ 40**	**$ 682,313**	**$ 2,432,793**	**$ (275,174)**	**$ 2,841,522**

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Amounts in Thousands

	Year Ended		
	January 30, 1999	January 31, 1998	February 1, 1997
Operating Activities:			
Net income	**$ 135,259**	$ 258,325	$238,621
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	**241,914**	201,410	195,186
Deferred income taxes	**(118,553)**	53,877	12,625
Changes in operating assets and liabilities:			
Decrease (increase) in accounts receivable, net	**110,103**	(28,178)	(26,929)
Decrease (increase) in merchandise inventories	**87,848**	(227,807)	(70,913)
Decrease (increase) in other current assets	**1,301**	(3,697)	1,083
Decrease (increase) in other assets	**12,647**	13,388	(23,852)
Increase (decrease) in trade accounts payable and accrued expenses and income taxes	**172,191**	(19,853)	(36,516)
Net cash provided by operating activities	**642,710**	247,465	289,305
Investing Activities:			
Purchase of property and equipment	**(248,485)**	(509,498)	(350,114)
Acquisition, net of cash acquired and assets held for sale	**(2,189,815)**	—	—
Net cash used in investing activities	**(2,438,300)**	(509,498)	(350,114)
Financing Activities:			
Net (decrease) increase in commercial paper	**(419,136)**	290,398	3,428
Proceeds from accounts receivable securitization	**300,000**	—	—
Proceeds from long-term borrowings	**1,650,000**	300,000	200,000
Proceeds from Guaranteed Preferred Beneficial Interests in the Company's Subordinated Debentures	**531,579**	—	—
Principal payments on long-term debt and capital lease obligations	**(134,442)**	(182,961)	(141,751)
Cash dividends paid	**(17,343)**	(17,930)	(11,360)
Proceeds from issuance of common stock	**25,183**	15,756	16,144
Purchase of treasury stock	**(109,683)**	(165,491)	—
Net cash provided by financing activities	**1,826,158**	239,772	66,461
Increase (Decrease) in Cash and Cash Equivalents	**30,568**	(22,261)	5,652
Cash and Cash Equivalents, Beginning of Year	**41,833**	64,094	58,442
Cash and Cash Equivalents, End of Year	**$ 72,401**	$ 41,833	$ 64,094

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Description of Business and Summary of Significant Accounting Policies

Description of Business – Dillard's, Inc. (the "Company") operates retail department stores located primarily in the Southeastern, Southwestern and Midwestern areas of the United States. The Company's fiscal year ends on the Saturday nearest January 31. Fiscal year 1998, 1997 and 1996 ended on January 30, 1999, January 31, 1998 and February 1, 1997, respectively, and included 52 weeks.

Consolidation – The accompanying consolidated financial statements include the accounts of Dillard's, Inc. and its wholly-owned subsidiaries. Intercompany accounts and transactions are eliminated in consolidation. Investments in and advances to joint ventures in which the Company has a 50% ownership interest are accounted for by the equity method.

Use of Estimates – The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash Equivalents – The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Accounts Receivable – Customer accounts receivable are classified as current assets and include some which are due after one year, consistent with industry practice. Concentrations of credit risk with respect to customer receivables are limited due to the large number of customers comprising the Company's credit card base, and their dispersion across the country.

In August 1998, the Company transferred, through a subsidiary, substantially all of its credit card receivables to a trust in exchange for a certificate representing an undivided interest in the trust. In January 1999, a Class A certificate with a market value of $300 million was sold to a third party. The Company owns the remaining undivided interest in the trust not represented by Class A certificates, which is classified in accounts receivable. The undivided interest in the trust represents securities that the Company intends to hold to maturity in accordance with Statement of Financial Accounting Standards ("SFAS") No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Due to the short-term revolving nature of the credit card portfolio, the carrying value of the Company's undivided interest in the trust approximates fair value. This transaction had no significant impact on the Company's earnings in fiscal 1998.

Merchandise Inventories – The retail last-in, first-out ("LIFO") inventory method is used to value merchandise inventories. At January 30, 1999 and January 31, 1998, the LIFO cost of merchandise was approximately equal to the first-in, first-out ("FIFO") cost of merchandise.

Property and Equipment – Property and equipment owned by the Company is stated at cost, which includes related interest costs incurred during the construction period, less accumulated depreciation and amortization. Capitalized interest was $3.1 million, $3.6 million and $4.4 million in fiscal 1998, 1997 and 1996, respectively. For tax reporting purposes, accelerated depreciation or cost recovery methods are used and the related deferred income taxes are included in noncurrent deferred income taxes in the consolidated balance sheets. For financial reporting purposes, depreciation is computed by the straight-line method over estimated useful lives:

Buildings and leasehold improvements	20 - 40 years
Furniture, fixtures and equipment	3 - 10 years

Properties leased by the Company under lease agreements which are determined to be capital leases are stated at an amount equal to the present value of the minimum lease

payments during the lease term, less accumulated amortization. The properties under capital leases and leasehold improvements under operating leases are being amortized on the straight-line method over the shorter of their useful lives or their related lease terms. The provision for amortization of leased properties is included in depreciation and amortization expense.

Goodwill – Goodwill, which represents the cost in excess of the fair value of net assets acquired, is amortized on the straight-line basis over 40 years.

The Company will assess the recoverability of the cost in excess of net assets acquired annually based on existing facts and circumstances and projected earnings before interest, depreciation and amortization on an undiscounted basis. Should the Company's assessment indicate an impairment of this asset in the future, an appropriate write-down will be recorded.

Revenue Recognition – The Company recognizes revenue at the "point of sale." Finance charge revenue earned on customer accounts, serviced by the Company under its private-label credit card program, is recognized in the period in which it is earned.

Advertising – Advertising and promotional costs, which include newspaper, television, radio and other media advertising, are expensed as incurred and were $220 million, $178 million and $168 million for fiscal year 1998, 1997 and 1996, respectively.

Store Preopening – Preopening costs of new stores are expensed in the quarter that the store opens. The adoption of the American Institute of Certified Public Accountants' Statement of Position (SOP) 98-5, "Reporting on the Costs of Start-Up Activities," in fiscal 1999, which will require such costs to be expensed as incurred, will not have a material impact on the results of operations.

Income Taxes – In accordance with SFAS No. 109, "Accounting for Income Taxes," deferred income taxes reflect the future tax consequences of differences between the tax bases of assets and liabilities and their financial reporting amounts at year-end.

Comprehensive Income – In February 1998, the Company adopted the provisions of SFAS No. 130, "Reporting Comprehensive Income," which is required for fiscal years beginning after December 15, 1997. Comprehensive income is equivalent to the Company's net income for fiscal years 1998, 1997 and 1996.

Segment Reporting – In February 1998, the Company adopted the provisions of SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information." SFAS No. 131 is effective for fiscal years beginning after December 15, 1997, and establishes standards for reporting information about a company's operating segments. It also establishes standards for related disclosures about products and services, geographic areas and major customers. The Company operates in a single operating segment — the operation of retail department stores. Revenues from external customers are derived from merchandise sales and service charges and interest on the Company's private-label credit card. The Company's merchandise sales mix by product category for the last three years was as follows:

Product Categories	1998	1997	1996
Cosmetics	**12.7%**	12.7%	12.9%
Women's and Juniors' Clothing	**30.7**	30.6	29.9
Children's Clothing	**6.6**	6.4	6.5
Men's Clothing and Accessories	**19.8**	19.5	19.5
Shoes, Accessories and Lingerie	**19.8**	20.2	19.9
Home	**9.5**	10.2	10.8
Leased Departments	**.9**	.4	.5
Total Merchandise Sales	**100.0%**	100.0%	100.0%

The Company does not rely on any major customers as a source of revenue.

Reclassification – Certain reclassifications have been made to prior-year financial statements to conform with fiscal 1998 presentation.

2. Acquisition

The Company completed its acquisition (the "Acquisition") of Mercantile Stores Company, Inc. ("Mercantile") on August 13, 1998 for a cash purchase price of approximately $3 billion. Mercantile was a conventional department store retailer engaged in the general merchandising business, operating 106 department and home fashion stores under 13 different names in a total of 17 states.

The Acquisition was accounted for under the purchase method and, accordingly, the results of operations have been included in the Company's results of operations since August 13, 1998, and the purchase price has been allocated to Mercantile's assets and liabilities based on their estimated fair values as of that date. The purchase price of $3 billion includes $2.95 billion of cash paid for stock, $30 million of investment banking and transaction costs, and $20 million of contractually obligated severance payments. The excess cost over the fair value of net assets acquired was allocated to goodwill. A total of $666 million was allocated to goodwill and will be amortized on a straight-line basis over 40 years.

In connection with the Acquisition, the Company entered into two separate agreements whereby the Company sold in the aggregate 26 of the acquired stores to Proffitt's, Inc. and The May Department Stores Company. In addition, the Company entered into an agreement with Belk, Inc. to exchange seven of the acquired stores for nine Belk, Inc. stores with a fair market value of approximately $70 million. The results of operations of the sold or exchanged stores are included in the accompanying statements of operations from the date of acquisition to the date of sale or exchange.

The following unaudited pro forma condensed statements of operations give effect to the Acquisition and related financing transactions as if such transactions had occurred at the beginning of the periods presented:

(in millions, except per share data)	**January 30, 1999**	January 31, 1998
Net sales	**$8,937**	$8,980
Net income	**111**	266
Basic income per share	**1.04**	2.39
Diluted income per share	**1.03**	2.38

The pro forma amounts reflect the results of operations of the Company, the acquired business and the following adjustments: (1) elimination of sales, cost of goods sold and operating expenses related to the stores subsequently sold, (2) depreciation on property and equipment and amortization of intangible assets based on the estimated purchase price allocation, (3) interest expense on the debt incurred in connection with the Acquisition, and (4) adjustment of income tax expense related to the above.

The foregoing unaudited pro forma information is provided for illustrative purposes only and does not purport to be indicative of results that actually would have been achieved had the Acquisition been consummated on the first day of the periods presented or of future results.

Subsequent to the Acquisition, the Company closed the Mercantile Corporate headquarters and consolidated six Mercantile distribution centers into existing operations. Included in advertising, selling, administrative and general expenses for fiscal 1998 were certain business integration expenses, including $43 million of severance costs and $26 million of lease rejection costs relating to facilities closed subsequent to the Acquisition. As of January 30, 1999, the Company paid approximately $45 million of such costs, and the remaining $24 million (primarily lease rejection costs) are included in the consolidated balance sheet in accrued expenses.

3. Commercial Paper and Revolving Credit Agreement

At January 30, 1999, there were no commercial paper borrowings outstanding. At January 31 1998, there were $419 million of commercial paper borrowings outstanding. At January 31, 1998, the weighted-average interest rate for outstanding commercial paper was 5.57%. The average amount of commercial paper outstanding during fiscal 1998 was $225 million, at a weighted-average interest rate of 5.75%. The average amount of commercial paper outstanding during fiscal 1997 was $244 million, at a weighted-average interest rate of 5.46%.

At January 30, 1999, the Company and a subsidiary, Dillard Investment Co., Inc. ("DIC"), had revolving line of credit agreements with various banks aggregating $750 million. The line of credit agreements require that consolidated stockholders' equity be maintained at $1 billion or more. These agreements expire on May 9, 2002. A commitment fee of .10% of the committed amount is paid to the banks to secure these line of credit agreements, which cannot be withdrawn except in the case of defaults by the Company or DIC. Interest may be fixed for periods from one to six months at the election of the Company or DIC. Interest is payable at the lead bank's certificate of deposit rate, alternative base rate or Eurodollar rate. There were no funds borrowed under the revolving line of credit agreements during fiscal 1996 through fiscal 1998.

4. Long-term Debt

Long-term debt consists of the following:

(in thousands of dollars)	**January 30, 1999**	January 31, 1998
Unsecured notes at rates ranging from 5.79% to 9.5%, due 1999 through 2028	**$3,007,000**	$1,300,000
Unsecured 9.25% note of DIC due 2001	**100,000**	100,000
Mortgage notes, payable monthly or quarterly (some with balloon payments) over periods up to 31 years from inception and bearing interest at rates ranging from 9.25% to 12.5%	**59,884**	72,984
	3,166,884	1,472,984
Current portion	**(164,289)**	(107,268)
	$3,002,595	$1,365,716

Building, land, land improvements and equipment with a carrying value of $81.7 million at January 30, 1999 are pledged as collateral on the mortgage notes.

Maturities of long-term debt over the next five years are $164.3 million, $108 million, $209 million, $109.9 million and $160.4 million.

Interest and debt expense consists of the following:

(in thousands of dollars)	**Fiscal 1998**	Fiscal 1997	Fiscal 1996
Long-term debt:			
Interest	**$202,571**	$118,466	$110,265
Amortization of debt expense	**2,243**	1,471	1,422
	204,814	119,937	111,687
Interest on capital lease obligations	**2,159**	1,626	1,813
Commercial paper interest	**4,707**	13,321	7,299
Other	**(15,000)**	(5,647)	(200)
	$196,680	$129,237	$120,599

Interest paid during fiscal 1998, 1997 and 1996 was approximately $149.3 million, $135.7 million and $129.4 million, respectively.

5. Trade Accounts Payable and Accrued Expenses

Trade accounts payable and accrued expenses consist of the following:

(in thousands of dollars)	**January 30, 1999**	January 31, 1998
Trade accounts payable	**$524,115**	$317,774
Accrued expenses:		
Taxes, other than income	**68,994**	48,497
Salaries, wages, and employee benefits	**98,857**	57,894
Interest	**90,796**	36,523
Rent	**42,112**	11,245
Other	**96,313**	58,101
	$921,187	$530,034

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
continued

6. Income Taxes

The provision for federal and state income taxes is summarized as follows:

(in thousands of dollars)	**Fiscal 1998**	Fiscal 1997	Fiscal 1996
Current:			
Federal	**$ 185,548**	$ 89,839	$117,230
State	**16,830**	7,994	10,285
	202,378	97,833	127,515
Deferred:			
Federal	**(108,657)**	49,292	11,310
State	**(9,896)**	4,585	1,315
	(118,553)	53,877	12,625
	$ 83,825	$151,710	$140,140

A reconciliation between income taxes computed using the effective income tax rate and the federal statutory income tax rate is presented below:

(in thousands of dollars)	**Fiscal 1998**	Fiscal 1997	Fiscal 1996
Income tax at the statutory federal rate	**$76,679**	$143,512	$132,377
State income taxes, net of federal benefit	**4,474**	8,176	7,584
Nondeductible goodwill amortization	**2,616**	—	—
Other	**56**	22	179
	$83,825	$151,710	$140,140

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred tax assets and liabilities as of January 30, 1999 and January 31, 1998 are as follows:

(in thousands of dollars)	**January 30, 1999**	January 31, 1998
Property and equipment bases and depreciation differences	**$506,820**	$264,526
State income taxes	**54,945**	24,018
Differences between book and tax basis of inventory	**33,577**	27,607
Pension asset differences	**93,110**	—
Joint venture bases differences	**36,608**	
Other	**16,675**	2,789
Total deferred tax liabilities	**741,735**	318,940
Accruals not currently deductible	**(37,598)**	(3,639)
State income taxes	**(3,410)**	(330)
Total deferred tax assets	**(41,008)**	(3,969)
Net deferred tax liabilities	**$700,727**	$314,971

Deferred tax assets and liabilities are presented as follows in the accompanying consolidated balance sheets:

(in thousands of dollars)	**January 30, 1999**	January 31, 1998
Current deferred tax liabilities	**$ 19,666**	$ 7,833
Noncurrent deferred tax liabilities	**681,061**	307,138
Net deferred tax liabilities	**$700,727**	$314,971

Income taxes paid during fiscal 1998, 1997 and 1996 were approximately $229.9 million, $100.0 million and $116.4 million, respectively.

7. Guaranteed Preferred Beneficial Interests in the Company's Subordinated Debentures

Guaranteed Preferred Beneficial Interests in the Company's Subordinated Debentures are comprised of $200 million liquidation amount of 7.5% Capital Securities, due August 1, 2038 (the "Capital Securities") representing beneficial ownership interest in the assets of Dillard's Capital Trust I, a wholly-owned subsidiary of the Company, and $331.6 million liquidation amount of LIBOR plus 1.56% Preferred Securities, due January 29, 2009 (the "Preferred Securities") by Horatio Finance V.O.F., a wholly-owned subsidiary of the Company.

Holders of the Capital Securities are entitled to receive cumulative cash distributions, payable quarterly, at the annual rate of 7.5% of the liquidation amount of $25 per Capital Security. The subordinated debentures are the sole asset of the Trust and the Capital Securities are subject to mandatory redemption upon repayment of the subordinated debentures.

Holders of the Preferred Securities are entitled to receive quarterly dividends at LIBOR plus 1.56%. The Preferred Securities are subject to mandatory redemption upon repayment of the debentures.

The Company's obligations under the debentures and related agreements, taken together, provide a full and unconditional guarantee of payments due on the Capital and Preferred Securities.

8. Benefit Plans

The Company has a retirement plan with a 401(k) salary deferral feature for eligible employees. Under the terms of the plan, employees may contribute up to 5% of gross earnings which will be matched 100% by the Company. The contributions are used to purchase Class A Common Stock of the Company for the account of the employee. The terms of the plan provide a five-year cliff-vesting schedule for the Company contribution to the plan. The costs to the Company for the 401(k) plan were $16 million, $14 million and $13 million for fiscal 1998, 1997 and 1996, respectively.

Mercantile maintained formal, qualified and non-qualified, non-contributory, defined benefit pension plans. In connection with the Acquisition, the Company froze the benefits accreting to the employees covered by the Plans, and applied to the applicable governmental authorities to distribute the benefits owed to each participant, in the form of lump-sum payments or non-participating annuity contracts, at the participant's election. In connection with the Acquisition, the Company recognized as prepaid pension costs all remaining unrecognized plan assets in excess of the actuarial present value of the benefit obligations. The following table sets forth the Plan's funded status and amounts recognized in the Company's consolidated balance sheet:

(in thousands of dollars)	**Fiscal 1998**
Actuarial present value of benefit obligation:	
Accumulated benefit obligation	**$227,721**
Projected benefit obligation	**227,721**
Plan assets at fair value, primarily money market investments	**422,011**
Plan assets in excess of accumulated benefit obligation (included in other assets)	**$194,290**

The weighted-average discount rate used in determining the actuarial present value of the benefit obligations was approximately 6.33%.

9. Stockholders' Equity

Capital stock is comprised of the following:

Type	Par Value	Shares Authorized
Preferred (5% cumulative)	$100	5,000
Additional preferred	$ .01	10,000,000
Class A, common	$ .01	289,000,000
Class B, common	$ .01	11,000,000

Holders of Class A are empowered as a class to elect one-third of the members of the Board of Directors and the holders of Class B are empowered as a class to elect two-thirds of the members of the Board of Directors. Shares of Class B are convertible at the option of any holder thereof into shares of Class A at the rate of one share of Class B for one share of Class A.

10. Earnings per Share

In accordance with SFAS No. 128, "Earnings Per Share," basic earnings per share has been computed based upon the weighted average of Class A and Class B common shares outstanding, after deducting preferred dividend requirements. Diluted earnings per share gives effect to outstanding stock options

Earnings per common share have been computed as follows:

(dollar amounts in thousands, except per share)	**Fiscal 1998** Basic	Diluted	Fiscal 1997 Basic	Diluted	Fiscal 1996 Basic	Diluted
Net income	**$135,259**	**$135,259**	$ 258,325	$ 258,325	$ 238,621	$ 238,621
Preferred stock dividends	**(22)**	**(22)**	(22)	(22)	(22)	(22)
Net earnings available for per-share calculation	**$135,237**	**$135,237**	$ 258,303	$ 258,303	$ 238,599	$ 238,599
Average shares common stock outstanding	**107,182**	**107,182**	111,303	111,303	113,482	113,482
Stock options		**454**		691		507
Total average equivalent shares	**107,182**	**107,636**	111,303	111,994	113,482	113,989
Earnings per share	**$ 1.26**	**$ 1.26**	$ 2.32	$ 2.31	$ 2.10	$ 2.09

Options to purchase 5,448,443, 2,618,406 and 4,806,120 shares of Class A Common Stock at prices ranging from $31.25 to $ 45.13 per share were outstanding in 1998, 1997 and 1996, respectively, but were not included in the computation of diluted earnings per share because the exercise price of the options exceed the average market price and would have been antidilutive.

11. Stock Options

The Company's 1998 Incentive and Nonqualified Stock Option Plan provides for the granting of options to purchase 6,000,000 shares of Class A Common Stock to certain key employees of the Company. Exercise and vesting terms for options granted under this plan are determined at each grant date. All options were granted at not less than fair market value at dates of grant. At the end of fiscal 1998, 3,864,120 shares were available for grant under the plan and 6,000,000 shares of Class A Common Stock were reserved for issuance under the 1998 stock option plan.

The Company's 1990 Incentive and Nonqualified Stock Option Plan provides for the granting of options to purchase 12 million shares of Class A Common Stock to certain key employees of the Company. Exercise and vesting terms for options granted under this plan are determined at each grant date. All options were granted at not less than fair market value at dates of grant. At the end of fiscal 1998, 1,974,662 shares were available for grant under the plan and 7,218,578 shares of Class A Common Stock were reserved for issuance under the 1990 stock option plan.

SFAS No. 123, "Accounting for Stock-Based Compensation," was effective for the Company for fiscal 1996. SFAS No. 123 encourages (but does not require) compensation expense to be measured based on the fair value of the equity instrument awarded. In accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," no compensation cost has been recognized in the consolidated statements of income for the Company's stock option plans. If compensation cost for the Company's stock option plans had been determined in accordance with the fair value method prescribed by SFAS No. 123, the Company's net income would have been $125 million, $245 million and $229 million for 1998, 1997 and 1996, respectively. Diluted earnings per share would have been $1.16, $2.18 and $2.01 for 1998, 1997 and 1996, respectively. Basic earnings per share would have been $1.16, $2.20 and $2.02 for 1998, 1997 and 1996, respectively. This pro forma information may not be representative of the amounts to be expected in future years as the fair value method of accounting prescribed by SFAS No. 123 has not been applied to options granted prior to 1995.

Stock option transactions are summarized as follows:

	Fiscal 1998		Fiscal 1997		Fiscal 1996	
Fixed Options	**Shares**	**Weighted-Average Exercise Price**	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding, beginning of year	**6,549,340**	**$ 33.25**	7,058,685	$ 33.85	6,448,006	$ 33.08
Granted	**2,155,880**	**37.24**	1,956,220	32.71	1,896,030	36.45
Exercised	**(931,687)**	**35.63**	(1,815,180)	32.92	(848,366)	31.69
Forfeited	**(393,737)**	**33.73**	(650,385)	39.05	(436,985)	37.91
Outstanding, end of year	**7,379,796**	**$ 33.83**	6,549,340	$ 33.25	7,058,685	$ 33.85
Options exercisable at year-end	**4,508,051**	**$ 34.09**	3,245,640	$ 32.41	3,079,350	$ 35.57
Weighted-average fair value of options granted during the year	**$8.80**		$7.78		$12.19	

The following table summarizes information about stock options outstanding at January 30, 1999:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Options Outstanding	Weighted-Average Remaining Contractual Life (Yrs.)	Weighted-Average Exercise Price	Options Exercisable	Weighted-Average Exercise Price
$27.25-$32.25	4,092,796	5.2	$ 29.88	2,382,901	$ 30.12
$37.00-$40.22	3,287,000	6.5	38.74	2,125,150	38.55
	7,379,796	5.8	$ 33.83	4,508,051	$ 34.09

The fair value of each option grant is estimated on the date of each grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants in 1998, 1997, and 1996, respectively: risk free interest rate 5.38%, 6.13% and 6.27%; expected life 3.1 years, 2.9 years and 4.3 years; expected volatility of 25.6%, 25.9% and 29.4%; dividend yield .44%, .49% and .38%. The fair values generated by the Black-Scholes model may not be indicative of the future benefit, if any, that may be received by the option holder.

12. Leases

Rental expense consists of the following:

(in thousands of dollars)	**Fiscal 1998**	Fiscal 1997	Fiscal 1996
Operating leases:			
Buildings:			
Minimum rentals	**$41,758**	$29,639	$28,842
Contingent rentals	**13,043**	11,863	12,482
Equipment	**11,545**	11,661	13,100
	66,346	53,163	54,424
Contingent rentals on capital leases	**1,636**	1,523	1,342
	$67,982	$54,686	$55,766

Contingent rentals on certain leases are based on a percentage of annual sales in excess of specified amounts. Other contingent rentals are based entirely on a percentage of sales.

The future minimum rental commitments as of January 30, 1999 for all noncancelable leases for buildings and equipment are as follows:

(in thousands of dollars) Fiscal Year	Operating Leases	Capital Leases
1999	$57,276	$5,120
2000	52,061	5,035
2001	47,437	4,674
2002	41,825	4,282
2003	36,522	3,991
After 2003	438,741	34,365
Total minimum lease payments	$673,862	$57,467
Less amount representing interest		(28,071)
Present value of net minimum lease payments (of which $2,396 is currently payable)		$ 29,396

Renewal options from three to 25 years exist on the majority of leased properties. At January 30, 1999, the Company is committed to incur costs of approximately $169.1 million to acquire, complete and furnish certain stores.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
continued

13. Fair Value Disclosures

The estimated fair values of financial instruments which are presented herein have been determined by the Company using available market information and appropriate valuation methodologies. However, considerable judgment is required in interpreting market data to develop estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of amounts the Company could realize in a current market exchange.

The fair value of trade accounts receivable is determined by discounting the estimated future cash flows at current market rates, after consideration of credit risks and servicing costs using historical rates. The fair value of the Company's long-term debt and Guaranteed Preferred Beneficial Interests in the Company's Subordinated Debentures is based on market prices or dealer quotes (for publicly traded unsecured notes) and on discounted future cash flows using current interest rates for financial instruments with similar characteristics and maturity (for bank notes and mortgage notes).

The fair value of the Company's cash and cash equivalents, trade accounts receivable and commercial paper borrowings approximates their carrying values at January 30, 1999 and January 31, 1998 due to the short-term maturities of these instruments. The fair value of the Company's long-term debt at January 30, 1999 and January 31, 1998 was $3,322 million and $1,618 million, respectively. The carrying value of the Company's long-term debt at January 30, 1999 and January 31, 1998 was $3,167 million and $1,473 million, respectively. The fair value and the carrying value of the Guaranteed Preferred Beneficial Interests in the Company's Subordinated Debentures at January 30, 1999 was $532 million.

14. Quarterly Results of Operations (unaudited)

The following is a tabulation of the unaudited quarterly results of operations for the years ended January 30, 1999 and January 31, 1998:

	Fiscal 1998, Three Months Ended			
(in thousands, except per share data)	**May 2**	**August 1**	**October 31**	**January 30**
Net sales	**$1,682,216**	**$1,504,504**	**$2,021,299**	**$2,588,722**
Gross profit	**564,995**	**540,360**	**653,033**	**820,258**
Net income	**63,070**	**47,946**	**(50,205)**	**74,448**
Basic earnings (loss) per share	**.58**	**.45**	**(.47)**	**.70**
Diluted earnings (loss) per share	**.58**	**.45**	**(.47)**	**.70**

	Fiscal 1997, Three Months Ended			
(in thousands, except per share data)	May 3	August 2	November 1	January 31
Net sales	$1,515,344	$1,453,152	$1,592,118	$2,071,138
Gross profit	520,141	507,033	535,815	675,472
Net income	58,258	44,342	44,347	111,378
Basic earnings per share	.52	.40	.40	1.01
Diluted earnings per share	.52	.40	.40	1.00

CORPORATE ORGANIZATION

William Dillard, II, *Chief Executive Officer*
Drue Corbusier, *Executive Vice President*
James I. Freeman, *Chief Financial Officer*
Alex Dillard, *President*
Mike Dillard, *Executive Vice President*
Paul J. Schroeder, Jr., *General Counsel*

Vice Presidents

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Gregg Athy
H. Gene Baker
Donald A. Bogart
Jan E. Bolton
Michael Bowen
Joseph P. Brennan
Kent Burnett
Larry Cailteux
Wynelle Chapman
James W. Cherry, Jr.
Neil Christensen
David M. Doub
Karl G. Ederer
T. R. Gastman
Walter C. Grammer
Randal L. Hankins
Marva Harrell
G. William Haviland
John Hawkins
Gene D. Heil
William L. Holder, Jr.
Dan W. Jensen
Mark Killingsworth
Gaston Lemoine
Denise Mahaffy
Robert G. McGushin
Paul E. McLynch
Michael S. McNiff
Jeff Menn
Anthony Menzie
Richard Moore
Cindy Myers-Ray
Steven K. Nelson
Steven T. Nicoll
Tom C. Patterson
Grizelda Reeder
Robin Sanderford
James Schatz
Linda Sholtis-Tucker
Terry Smith
Burt Squires
Sandra Steinberg
Joseph W. Story
Ralph Stuart
Tom Sullivan
Julie A. Taylor
David Terry
Paul Thum Suden
Charles O. Unfried
Richard Vasey
Keith White
Ronald Wiggins
Kent Wiley
Richard B. Willey
Gary Wirth
Linda Zwern

Merchandising Division Management

Ft. Worth Division

Drue Corbusier
President

Gregg Athy
Vice President, Merchandising

Wynelle Chapman
Vice President, Merchandising

William B. Warner
Director of Sales Promotion

Little Rock Division

Mike Dillard
President

David Terry
Vice President, Merchandising

Keith White
Vice President, Merchandising

Ken Eaton
Director of Sales Promotion

Louisville Division

Robin Sanderford
President

Ronald Wiggins
Vice President, Merchandising

Sandra Gudorf
Director of Sales Promotion

Phoenix Division

Kent Burnett
President

Julie A. Taylor
Vice President, Merchandising

Tom Sullivan
Vice President, Merchandising

Robert E. Baker
Director of Sales Promotion

St. Louis Division

Joseph P. Brennan
President

Mark Killingsworth
Vice President, Merchandising

Mark Gastman
Director of Sales Promotion

Tampa Division

David Doub
President

Linda Zwern
Vice President, Merchandising

Louise Platt
Director of Sales Promotion

CORPORATE ORGANIZATION

Board of Directors

William Dillard
Chairman of the Board

Calvin N. Clyde, Jr.
Chairman of the Board
T.B. Butler Publishing Co., Inc.
Tyler, Texas

Robert C. Connor
Investments

Drue Corbusier
Executive Vice President
Dillard's, Inc.

Will D. Davis
Partner
Heath, Davis & McCalla, Attorneys
Austin, Texas

Alex Dillard
President
Dillard's, Inc.

Mike Dillard
Executive Vice President
Dillard's, Inc.

William Dillard, II
Chief Executive Officer
Dillard's, Inc.

James I. Freeman
Senior Vice President
Chief Financial Officer
Dillard's, Inc.

John Paul Hammerschmidt
Retired Member of Congress
Harrison, Arkansas

William B. Harrison, Jr.
Vice Chairman
Chase Manhattan Corporation
New York, New York

John H. Johnson
President and Publisher
Johnson Publishing Company, Inc.
Chicago, Illinois

E. Ray Kemp
Retired Vice Chairman and Chief Administrative Officer
Dillard's, Inc.

Jackson T. Stephens
Chairman
Stephens Group, Inc.
Little Rock, Arkansas

William H. Sutton
Managing Partner
Friday, Eldredge & Clark, Attorneys
Little Rock, Arkansas

Standing, left to right:
James I. Freeman, Calvin N. Clyde, Jr., William H. Sutton, Mike Dillard, William B. Harrison, Jr., Drue Corbusier, William Dillard, II, Robert C. Connor, Will D. Davis and John Paul Hammerschmidt

Seated, left to right:
Alex Dillard, John H. Johnson, William Dillard, Jackson T. Stephens and E. Ray Kemp

SHAREHOLDER INFORMATION

Annual Meeting
Saturday, May 15, 1999, at 9:30 a.m., Auditorium, Dillard's Corporate Office, 1600 Cantrell Road, Little Rock, Arkansas 72201

Form 10-K
Copies of the Company's 10-K Annual Report may be obtained by written request to: James I. Freeman, Senior Vice President and Chief Financial Officer, Post Office Box 486, Little Rock, Arkansas 72203

Corporate Headquarters
1600 Cantrell Road, Little Rock, Arkansas 72201

Mailing Address
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Telex: 910-722-7322
Fax: 501-376-5917

Transfer Agent and Registrar
Chase Mellon, 85 Challenger Road, Overpeck Centre, Ridgefield Park, New Jersey 07660

Listing
New York Stock Exchange Ticker Symbol: DDS

Stock Prices and Dividends by Quarter

	1998		1997		Dividends per Share	
	High	Low	High	Low	1998	1997
First	$39.63	$34.94	$32.50	$28.00	$0.04	$0.04
Second	44.50	32.81	38.06	30.63	0.04	0.04
Third	37.06	26.50	44.75	34.00	0.04	0.04
Fourth	36.25	24.75	41.38	32.56	0.04	0.04

Dillard's

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